

## WHEN IS A NOTE FRAUDULENT?

When it comes to investment fraud, promissory notes have become a favorite among con artists. Unfortunately, promissory notes are generally touted to unsuspecting investors who are enticed by the outrageous promises accompanying the notes. These notes are sold as instruments that guarantee above-market, fixed interest rates, while safeguarding the principal amounts invested.

Although promissory notes can be appropriate investments for many individuals, they are increasingly being used as vehicles to defraud investors out of millions of dollars and have become a growing problem for regulators. Promissory notes are often sold by insurance agents who may not realize they must be licensed as securities brokers to sell the notes. The person promoting the notes may have limited information, other than what the company offering the notes has told him/her. Even worse, sometimes what little information the agent does have is not completely accurate. Some notes are issued on behalf of companies that do not even exist. The agents who offer these notes are often lured by the promise of high commissions for promotion and sales.

The crimes-of-persuasion Web site reminds investors, "You would be wise to remember that a promissory note is only as good as the promise which backs it. Investors often receive fabricated promissory note certificates complete with fiscal and legal-sounding terminology and gold embossed seals" ([www.crimes-of-persuasion.com](http://www.crimes-of-persuasion.com)). Be wary of these opportunities that often play the high-reward-with-low-risk card. **If it sounds too good to be true, it probably is.** According to the North American Securities Administrators Association (NASAA), 35 states have reported complaints or brought enforcement actions involving promissory notes. Promissory notes have been frequently listed on the annually released NASAA "Top Ten Investment Scams" list. You can find the "Top Ten Investment Scams" list along with other information on NASAA's web site at [www.NASAA.org](http://www.NASAA.org)

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Promissory Notes

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## WHAT IS A PROMISSORY NOTE?

A promissory note is a written promise to pay a sum of money to a specific person at a particular time in the future. In investment terms, this usually means that a company has issued a note stating that its investors will receive a return on their investments in a set amount of time. This type of note typically involves a loan to a company made by an investor in exchange for a fixed amount of periodic income.



Promissory notes are a form of debt similar to a loan. Companies issue these notes to finance any aspect of their business, from launching new products to repaying more expensive debt. In return for the loan, companies agree to pay investors a fixed return over a set period of time.

Promissory notes are an important means by which companies raise capital. Legitimate promissory notes are marketed almost exclusively to sophisticated or corporate investors who have the resources to thoroughly research the companies issuing the notes, and to determine whether the issuers have the capacity to pay the promised interest and principal.

## HOW CAN NOTE FRAUD BE AVOIDED?

Registration is important because the process involves what is known as "due diligence." In short, due diligence means that financial professionals, including lawyers and accountants, have reviewed the notes and companies behind the notes. While due diligence does not guarantee that you will be repaid, it means that you are much more likely to be given accurate information that will help you make an informed decision. There is a difference between getting into risky investments and those which are fraudulent.



When dealing with promissory notes, it is most important to remember that notes are a high-risk investment opportunity, even when they are legitimate. Before investing, an individual should always make sure that he/she has all available information about the investment. The investor should also always call Indiana Secretary of State Todd Rokita's office at **800.223.8791** to make sure that the investment is registered. If a promissory note is exempt from registration, Secretary Rokita's office will be able to indicate that as well. When making this call, the investor should also check on the agent selling the investment. All agents selling securities in the state of Indiana must be registered with Indiana Secretary of State Todd Rokita's office. While we cannot guarantee the safety of an investment, we can tell you if the security and the agent selling the security are registered.

## WHO CAN HELP VICTIMS OF NOTE FRAUD?

Most promissory notes must be registered as securities with the Securities and Exchange Commission and the regulatory offices of the states where they are being sold. It is important to remember, however, that some promissory notes, such as those that have nine-month or shorter terms, may be exempt from registration. Since these notes fly under the radar screen of securities regulatory review, they have been the major source of investor complaints and fraudulent activity.

The sales people who market promissory notes typically include securities brokers, insurance agents, financial planners and investment advisers. Since promissory notes are securities, they must be sold by salespeople who have the appropriate securities license or registration.

